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SENSITIVE

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TREASURY FOR RON BLOOM AND JEFF BAKER

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SUBJECT: OPEL SALE COLLIDES WITH POLITICS

¶1. (SBU) SUMMARY. Always be prepared for the unexpected: that might be the moral of the story in the German Opel deal so far. Just as the independent new GM-Europe trust fund was expected to announce its decision on the complex sale of 55 percent of General Motors' (GM's) holdings in the car maker, the German board members of the Trust - appointed by the German federal government and the four German states (Laender) with Opel plants - threw a wrench in the works by voting against the deal favored by the German state and federal governments. For weeks the GM Europe trust fund ("Treuhand") board has examined proposals from potential investors, with the field narrowed to two contenders: Magna/Sberbank and RHJ (Ripplewood). The Chancellery and the four Laender had made it crystal clear that they favored Magna's offer because it would allegedly save more jobs. Although details of the board's July 22 deliberations were not made public, the government announced that the deal was deadlocked. What is more, the press reported that one of the trust's two German government members had joined the two GM reps in favor of Ripplewood, whereas the other called for outright insolvency, i.e., the dissolution of Opel.

¶2. (SBU) Meanwhile, the German government is keeping Opel afloat for up to six months with a 1.5 billion euro bridge loan, and has pledged up to 3.0 billion euro in additional loan guarantees to the "New Opel" expected to emerge from this process. Once the Treuhand selects an investor, new negotiations involving the governments of countries hosting other GM-Europe operations will commence to determine how much assistance they are prepared to offer - and indirectly, how many plants and jobs will be saved in those countries. Despite the large amounts of financing needed and the risky stakes, German government interlocutors seem confident that Opel will emerge as a stronger company and that German government funds will not be lost. END SUMMARY.

A Complex Deal

¶3. (U) General Motors (GM) has offered 55 percent of its Europe holdings to investors and will retain 35 percent as a minority stockholder. (Opel workers and dealers would presumably take 10 percent.) These include holdings in Opel (with plants primarily in four states in Germany, and operations in Spain, Poland, and Belgium), as well as Vauxhall in the UK. The new investor will combine these operations into a newly restructured, leaner company. GM holdings in Saab have already been sold, and almost everyone believes the plant in Antwerp will close. The deal was supposed to be completed as early as this week, but now will probably be pushed into August.

¶4. (U) The German media has been obsessed with the fate of Opel and its connection with GM, releasing daily reports of

varying quality and veracity. To better ascertain what is happening, EMIN and Econoff met with Fred Irwin, Chairman of the GM Europe Trust, Jochen Homann, State Secretary in the Ministry of Economics and head of the German Government's Opel Task Force, and Winfried Horstmann, Chancellor Merkel's advisor on industry including Opel, and others.

Who Makes the Decision?

¶5. (SBU) Three potential investors have presented proposals: the Canadian Auto Parts Manufacturer Magna (in association with Russian Sberbank and Gaz, a car maker), the international investment firm RHJ(I) (a.k.a. Ripplewood), and the Chinese Auto Company BAIC. Press reports on July 24 confirm that BAIC is no longer under consideration.

¶6. (U) Although the Trust is supposed to decide which proposal to accept, no single entity will make the final call. GM has placed those shares to be sold into the Trust, whose Board has five members, one from GM Detroit, one from GM Europe, one member representing the four state governments in which Opel plants are located (Thuringia, Nord Rhine Westfalen, Hesse, and Rhineland Pfalz), and the German government. The 5th member, German AmCham President and Citigroup country manager Fred Irwin, is the Trust's nonvoting President. Irwin explained to us that the Trust will not take a binding vote until it can reach a consensus among all the parties involved.

¶7. (U) On July 22, the GM Board members presented their

preference to the full Board and representatives of the German Government. Press reports indicate that GM was leaning toward RHJ(I), but may not make an announcement until it conducts its Supervisory Board meeting on the Opel issue on August 3. Irwin told the Embassy that he had urged the GM representatives on the Trust Board to first inform the other Board members and consult with the German federal and state governments before going to GM Headquarters with its proposal. The entirely unexpected decision by the German Board members to turn against Magna, if true, means that there is likely to be considerable wheeling and dealing in the days and possibly weeks ahead.

The Role of the Four States

¶8. (U) Originally, the conventional thinking was that a restructured Opel would require the closing of at least one or two German plants. Yet the governments of the four German states with Opel interests, focused entirely on keeping their Opel plants open and preserving much- needed jobs, managed to shift the equation. By contributing half of the 1.5 billion euro "bridge fund" to keep Opel in operation (Berlin contributed the other half), the Laender gained leverage in the negotiations, meaning that almost unnoticed, the Magna and (it appears) Ripplewood deals no longer spoke of closing any plants whatsoever. Until a new investor can take over and arrange sufficient funding, the state and federal governments are each contributing 50 percent, with the contributions as follows: Federal Government 750 million euros, Hessen 447 million euro, NRW 150 million euros, Rhineland Pfalz 102 million euro and Thuringia 51 million euro.

¶9. (SBU) Thuringia, home to Opel's state of the art Eisenach auto plant and a technological symbol of the new eastern Germany, is a case in point. German press reports originally indicated that the RHJ(I) wanted to mothball Eisenach for two years, prompting loud complaints from locals who feared that would mean permanent closure. The press (and auto industry representatives whom we interviewed) likewise

had confidently predicted that Hesse's Kaiserslautern plant would be shuttered. By the time we met with the Chancellery's Horstmann on July 22, however, he could confirm that these plans have since been dropped and that all three proposals (including BAIC) would keep every German Opel plant up and running. The Laender reportedly have a strong preference for the Magna proposal, partly due to suspicion of foreign "hedge funds" like Ripplewood.

Protecting Intellectual Property

¶10. (SBU) All of our interlocutors confirmed that intellectual property (IP) was a key sticking point in these negotiations. GM holds the rights to Opel IP, much of which originated at the Russelsheim facility, which employs 3,000 technicians and engineers. The German press repeatedly alleged that GM did not really own these rights, having purchased them from Opel with promissory notes that it never honored. Horstmann and Homann both alluded to these stories, but confirmed that the German government has chosen to set these concerns aside in the interests of a smooth and quick sale. Irwin and others confirmed that GM would provide funding to keep the Russelsheim R&D facility in operation and save 3,000 jobs. In return, the new investor would pay royalties to GM at below the accepted market rate of 5 percent, perhaps 3.5 to 3.8 percent, returning to 5 percent after several years.

¶11. (SBU) GM was reportedly concerned that Russian involvement in the Magna proposal could allow a competitor to gain access to sensitive IP developed at great cost. German government interlocutors played down this danger. In their view, while a Chinese bid would cause serious concern, the new Opel would be able to restrict Russian access to IP (one source added that Russian firms are more "trustworthy" than the Chinese.)

Is the German Government Divided?

¶12. (U) The German press has described serious disagreements within the German government on the Opel sale.

The state governments and the SPD, backed by the labor unions, are purportedly strongly behind the Magna bid, as they believe RHJ(I)intends to gut Opel and sell it back to GM at quick profit. They further allege that RHJ(I) does not have the expertise to manage an auto company and would repeat management "mistakes" committed by GM.

¶13. Economic Minister zu Guttenberg -- who represents the more entrepreneurial Bavarian partner (CSU) to Merkel's CDU opposed an Opel rescue from the start and considered a controlled insolvency a better option. Nonetheless, zu Guttenberg has lately maintained near total silence on the matter, and his deputy, State Secretary Homann who heads the government's task force on Opel, made on the record statements this week supporting the Magna bid. The Chancellor's office was also fairly agnostic, but this week Merkel's spokesman and trusted advisor, Ulrich Wilhelm, came out clearly in favor of Magna as well.

Blaming GM

¶14. (SBU) For months, most newspapers here have blamed GM for running a 'perfectly good German company' into the ground. The predominant sentiment was that Opel should make a clean and total break from GM, and many worried that GM would attempt to repurchase the company once it recovers with German taxpayers' help. Cooler heads prevailed, however, and

now almost everyone realizes that Opel can only survive as part of a restructured GM-Europe entity.

¶15. (SBU) The Economic Ministry confirmed to us that the German government has pledged 3.0 billion euro in loan guarantees to the "New Opel" until 2016. This figure, when combined with the 1.5 billion euro bridge loan guarantee means 4.5 billion of potential German government assistance available to the new investor. Both Homann and Horstmann were confident that the new company would survive, and that despite the obvious risks, both were confident that the German government would not lose money.

HOW TO CUT

¶16. (SBU) The restructuring will undoubtedly be painful. Opel/Vauxhall employs just over 50,000 people throughout Europe, with 25,000 in Germany. Everyone seems to agree that no matter which proposal is accepted, some 10,000 jobs will be lost, of which perhaps 7500 will come from Germany. Naturally, German politicians want to keep job losses in Germany to an absolute minimum. The Minister Presidents of the concerned states lobbied effectively and ensured that no proposal would close a German plant; instead, the losses will spread out over all four factories.

¶17. (SBU) With a national election looming in September, Opel has emerged as an obvious campaign issue. The German government is determined to conclude the sale before elections begin, so as to deny the opposition a potential campaign issue. Horstmann predicted that if the process became protracted and drifted into the campaign season, the SPD would surely use it against the CDU. SPD candidate for Chancellor Frank Walter Steinmeier, the Vice Chancellor and Foreign Minister, has been an outspoken proponent of the Magna bid, and argued that the 4.5 billion state aid should only be available to Magna.

The Role of Other Governments

¶18. (SBU) As soon as the Treuhand accepts an investment proposal, we heard, an entirely new process will begin, as negotiations expand to include other governments. These talks will be at least as complicated as the intra-German discussions.

¶19. (SBU) Almost all sources indicate that the Opel plant in Antwerp, Belgium is likely to close regardless of which proposal is accepted. Horstmann and Homann, for instance, confirmed that the Belgian government has accepted the inevitable, and does not intend to try to save this plant by putting up lots of its own money. German interlocutors indicated that the Spanish government has stated its interest in keeping the Opel plant in Zaragoza open and is

willing to commit public money to do so. We know less about the Opel plant in Gliwice, but understand that it is modern, state of the art, efficient, and unlikely to be closed. Press reports and British sources in Berlin say that organized labor is determined to keep Vauxhall plants open and that the government may provide (undisclosed) funds for this purpose although job cuts are inevitable.

¶20. (SBU) For their part, Horstmann and Homann informed us that the governments of Spain and the UK will come forward with their own financial packages as soon as an investor is named. They were less certain about Poland. Both Horstmann and Homann pointed out that the 3.0 billion euros in loan guarantees pledged by Germany did not reflect the contribution of other governments; as soon as London and Madrid put their own funds on the table, Germany's financial

liability would be reduced. They pointed out that in any case, these are loan guarantees rather than actual expenditures and would help procure commercial lending for the New Opel at lower rates. German funds would only be expended if Opel defaulted.

Comment

¶21. (SBU) The German government has presented a happy face to us regarding these complex negotiations although in our view, the process is fraught with risk. Germany has placed 4.5 billion euro on the table, while potential private investors would bring relatively little of their own money and would need commercial loans at a time when money is tight. Although German officials appear confident about Opel's quick recovery, Opel has been bleeding large amounts of money for some time and could require considerable investment before it is safely on its feet. Pressure from the German state governments and organized labor could also tie the hands of an investor, as it now appears that any closure of German plants has been ruled out. In the end, the German government may find itself taking on more than it bargained for.
Bradtke